Memorandum for:

Attached are various unclassified economic studies on the West German economy and classified model simulations analyzing the impact on West German economic activity of alternative growth in world demand and government investment scenarios. The data were requested by George W. Bader, Deputy Principal Director for European Policy, Office of the Secretary of Defense.

[redacted]

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2 May 1984

Director,

EURA

Office of European Analysis

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1 May 1984

MEMORANDUM FOR: George W. Bader
Deputy Principal Director for European Policy
Office of the Assistant Secretary of Defense

FROM : 25X1
Chief, Western Europe Division
Office of European Analysis

SUBJECT : West German Economic Data

1. In response to your request, attached are copies of a number of unclassified studies and statistical data on West German economic activity. We also have prepared nine sets of tables summarizing the impact that various levels of government investment and world demand could have on West German economic growth in the medium term. We used our model of the West German economy to prepare a baseline forecast through 1987 and to simulate world growth and alternative government investment patterns. 25X1

2. The model simulations are as follows:

-- Set 1: Baseline Forecast

The control solution assumes world demand, excluding West Germany, will grow an average of almost 5 percent in the 1984-87 period. Government investment increases by slightly over 2 percent, within bounds dictated by the Finance Ministry and below the anticipated real GNP growth rate.

-- Set 2: Low- growth scenario

World demand growth averages less than 3 percent in the forecast period.

-- Set 3: High-growth scenario

Pickup in world demand is greater than anticipated, with growth averaging over 7 percent.

-- Set 4: Sharp increase in government investment

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Government boosts investment in construction by $5 billion in each forecast year.

-- Set 5: Low growth scenario combined with $5 billion permanent increase in public construction investment.

-- Set 6: High growth scenario combined with $5 billion permanent increase in public construction investment.

-- Set 7: Moderate increase in government investment

Government increases investment in construction by DM2 billion ($800 million) in each forecast year.

-- Set 8: Low-growth scenario combined with DM2 billion permanent increase in public construction investment.

-- Set 9: High-growth scenario combined with DM2 billion permanent increase in public construction investment.

Each set contains 11 tables. Tables 10 and 11 list exogenous variables, consisting mainly of fiscal and monetary policy options and external shocks to the economy. [redacted] 25X1

3. At least a $5 billion (DM12 billion) permanent increase in government investment would be required to have significant impact on West German economic growth. An investment in construction of this size would cause GNP to jump by almost one percentage point in 1984 over the baseline case. GNP growth for 1985, 1986, and 1987 would only match the baseline forecast in terms of real growth rates although the economy would be functioning at a higher level. Unemployment would fall by over 9 percent during the period (with the unemployment rate dropping about one percentage point). [redacted] 25X1

4. On the negative side, the model shows that the net public deficit would increase significantly -- assuming that tax policy would remain constant -- and the current account surplus would fall slightly. The initial increase in imports of goods and services probably is overstated, however, in that a proportionately larger amount of materials used by the construction industry could be supplied by the domestic market and not imported as the model indicates. Our model cannot make this distinction since imports and exports are not broken out by commodity. [redacted] 25X1

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5. A more realistic increase in government construction investment of DM2 billion for each of the years has little impact on economic activity. The level of real GNP rises by only 0.1 percent over the baseline forecast. Unemployment improves only slightly; the impact on the current account surplus and budget deficit is minimal as well. As expected, increased spending would have a more pronounced impact at a time of weak world demand.

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